Investor Relations Meeting for 1H of FY2023
Q&A Summary

Presenters
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Q1. Please describe the momentum of fee businesses. Although the most recent results of fee income seem to be somewhat weaker, do you think their results are in line with your plans? For the Resona Group to achieve the targets of its medium-term management plan (MMP), it needs to raise fee income in the second year of the MMP and later. Could you share the status of progress in your efforts in this regard?

A1. In the first half of FY2023, settlement-related income remained firm. Also, results were stable for debit cards, electronic banking (EB), domestic exchange and other solutions designed to meet customer needs associated with corporate transactions or household finance. In addition, we have made steady progress in such initiatives as the integration of face-to-face and digital channels.

On the other hand, income of succession-related businesses declined due in part to the absence of major deals, like those recorded in the previous fiscal year in connection with real estate, M&A and other fields. However, in the aftermath of the COVID-19 pandemic, we have seen the emergence of needs for solutions supporting the smooth succession of businesses and assets to next-generation owners. In this light, we are confident about our future ability to seize opportunities arising from this demand. In fact, the current volume of potential deals in our pipelines is in excess of the volume seen in the same period of the previous fiscal year.

We therefore hope to report robust results for FY2023, the first year of the MMP, upon achieving our annual targets. We believe that the actual momentum of our operations is stronger than what people outside the Group might perceive.

Q2. Please elaborate on the shift of funds from the Bank of Japan (BOJ)'s current account deposits to Japanese government bond (JGB) investments. Although the balance of available-for-sale securities and held-to-maturity bonds has not increased substantially in the first half, do you intend to increase this balance at a faster pace going forward? If that is the case, do you intend to raise the volume of JGB investments by allocating more funds to available-for-sale securities with maturities of around five years and held-to-maturity bonds with maturities of around 10 years? Please comment on your future investment strategies.

A2. Previously, we have focused on holding bonds with longer maturity, such as 20-year bonds, even as we maintain bonds with shorter maturities, in line with our objective of securing a certain volume of carry-trading profit in an environment with extremely low interest rates. This approach resulted in a “dumbbell” portfolio.

However, we are now seeing signs of changes in the yen-bond interest rate environment. Against this backdrop, we implemented considerable hedging measures for 20-year bonds and other bond holdings prior to the announcement of the BOJ’s new policy of allowing greater flexibility in yield curve control (YCC) in July 2023. Thus, we have promoted preparatory steps to ensure our readiness to risk-taking endeavors.

Currently, we believe that a yen-bond portfolio equipped with a robust volume of bonds with medium range maturity is desirable. If interest rate trends remain murky going forward, we may continue to increase our holdings of such bonds even though they could bring us a certain volume of unrealized losses. Although we are now striving to acquire such instruments as held-to-maturity bonds, we feel that we are getting close to timing when we accelerate the pace of acquisition while paying close attention to changes in interest rate trends.

Q3: With regard to loans and bills discounted, the momentum of loan balance in the first half seems to be somewhat weak. Could you please comment on this?

A3: We feel that the momentum of corporate loans for business corporations has been strong. For example, the average balance of corporate loans in the first half grew 3.0% year on year. This outpaced the 1.5% year-on-year growth recorded in the same period of the previous fiscal year.

While the economy is in a recovery phase from fallout from the COVID-19 pandemic, the macro environment is being altered by the progressing aging of society, a declining birthrate, climate change and other factors. Reflecting this, customer needs are becoming ever more diverse, requiring ever more sophisticated solutions. The Resona Group is capable of extending a growing volume of lending to a diverse range of borrowers by delivering consulting services finely tuned to accommodate each customer. We will allocate additional staff and other management resources to this area and otherwise implement robust measures to achieve our MMP targets.

Q4. It looks like the volume of housing loan origination has been somewhat weak. Please comment on your recognition of the environment surrounding the housing loan business and the Group’s future policy on the development of this business.

A4. In light of such factors as surges in property prices, the overall status of the housing loan market currently lacks momentum. However, we maintain a housing loan balance of nearly JPY14 trillion. In this field, we have particular strength backed by expertise and know-how amassed in the course of extending housing loans for many years. In addition, we have developed web-based loan procedures and other mechanisms. Leveraging these and other assets, we can operate the housing loan business at lower costs.

Our conventional strength also lies in channels arising from our relationships with housing companies. Furthermore, we have seen progress in our efforts to strengthen the direct approach to end-users. With a growing number of customers now using our Group App, we are also becoming capable of assessing behavioral patterns of customers. This is yet another source of our considerable advantage in housing loans.

Previously, our contact points with housing loan customers have, on many occasions, ended at the signing of housing loan contracts. Today, however, we are able to secure ongoing contact points with customers via the Group App even after the origination of housing loans. These contact points, in turn, enable us to take a data-driven business development approach backed by transactional data. Therefore, income per customer is very likely to remain robust as it derives from a broader range of transactions over a long period of time. Overall, our housing loan business has growth potential in many respects.

Q5. With regard to the restructuring of the yen interest rate portfolio, could you please elaborate on the future direction of your initiatives in light of the recent trend in the BOJ's monetary policies since the formulation of the MMP?

A5. We formulated the current MMP without factoring in the effect of interest rate rises. On the other hand, the recent trends of BOJ's YCC policy and the growing probability of normalization of its monetary policies could possibly change our business environment. Given these factors, we think that we will very likely be able to implement additional risk-taking endeavors and allocate a greater volume of funds than planned to our yen interest rate portfolio by leveraging our low-margin deposit base with strong retention.

Q6. Recently, the Resona Group announced its decision to convert two lease companies into consolidated subsidiaries. The current estimate indicates that the Group will be able to additionally invest approximately JPY90.0 billion during the course of the MMP period to achieve inorganic growth. Please once again elaborate on your policy regarding inorganic investment.

A6. As the first step of our inorganic strategies under the MMP, we consider the consolidation of the two lease companies a quite successful move. While we have seen robust needs for leasing among SME customers, leasing itself has strong affinity with banking. Accordingly, we believe that we will be able to swiftly raise profit from these subsidiaries to a certain level by taking advantage of a combination of their leasing functions with the Group's customer base consisting of 500,000 corporate customers.

As the Resona Group entered a new phase of effective capital utilization, we don't want to heavily limit our future options regarding inorganic strategies. Starting with discussing “what value we can deliver to customers,” we aim to utilize capital to enhance our customer base, management resources and functions. We are open to utilizing capital in a variety of fields. In particular, we have seen strong customer needs in fields related to financing, digital technology, data utilization, settlement and other undertakings. These fields are also highly relevant to our current business portfolio. Although opportunities available to us going forward may depend on prevailing circumstances, we will robustly strive to expand the scope of strategic business alliances.

Q7. Please explain the status of loans to SMEs (page 13 of the IR presentation material), especially matters regarding trends of funding demand and preparatory measures currently undertaken with an eye to adapting to hikes in interest rates.

A7. The volume of funding we extend to support capital expenditures is now growing. Also, the volume of funds extended in SX-related retail transition financing has grown around twofold compared with the same period of the previous fiscal year. In sum, the volume of lending is on a growth track on the back of the diversification of needs among customers for ever more sophisticated solutions.

During our presentations, we have touched on our policy of pursuing the “best mix of profit.” Previously, we have focused on raising fee income and reducing costs in order to promote income and cost structure reforms amid an extremely low interest rate environment. However, when interest rate rise, we will be able to leverage our deposit and lending businesses to make a major positive impact on society.

Q8. Please elaborate on the merger of KMFG by Resona Holdings (HD), which is described on page 18 of the IR presentation material. What is the purpose of launching yet another measure aimed at strengthening Group governance at this timing?

A8. Immediately after the inauguration of KMFG in 2018, Kansai Urban Banking Corporation and The Kinki Osaka Bank, Limited were merged, and the integration of their back-office systems was completed a year later. Based on this success, we recognize that the reorganization of KMFG subsidiaries has been much needed. KMFG’s annual contribution to consolidated profit has increased from JPY6.0 billion to JPY22.2 billion over the course of five years since becoming a Resona Group member. As such, KMFG has played a robust part in realizing synergies, both in terms of top-line income growth and cost reduction, during the initial phase of reorganization.

On the other hand, we now see changes taking place at an ever-faster pace. As we aim to achieve the further strengthening of consolidated Group management in line with the MMP, we need to raise our capabilities for speed-oriented decision making while decisively pursuing a “one-platform, multi-regional strategy” in which our four Group banks implement their own sales strategies aligned with region-specific circumstances even as they operate on a unified platform that integrates back-office operations and indirect departments. These were the thoughts behind our recent decision to merge KMFG.

Q9. Please share your assessment of expenses incurred by KMFG and the future outlook on this subject.

Also, we have heard that the statutory corporate tax rate applied to Kansai Mirai Bank (KMB) was downwardly revised in the first quarter. Will the merger of HD and KMFG have any impact on this tax rate revision?

A9. We think that KMFG's expenses could be reduced further on a non-consolidated basis. Our plans also call for the integration of Minato Bank's back-office systems. Moreover, our "one-platform, multi-regional strategy" will enable us to execute additional cost reduction measures. These factors will also help Resona Bank (RB) and Saitama Resona Bank (SR) achieve cost reductions on their own. Although the current cost income ratio remains somewhat high, we aim to ensure that our upfront investment yields robust outcomes at some point in time in the near future.

Tax effects available to KMB are attributable to the recording of deferred tax assets in connection with tax loss scheduling for loans and bills discounted. The materialization of these tax effects was achieved by KMB alone and is unrelated to the reorganization measure we have announced earlier. Moreover, these effects will remain over the course of FY2023.

Generally speaking, the merger of HD and KMFG has no financial impact. Although HD will recognize gains on extinguishment of tie-in shares on a non-consolidated basis, these gains are expected to be offset on a consolidated basis. Accordingly, there will be no impact on HD's consolidated operating results.

Q10. Please elaborate on your concepts behind the total shareholder return ratio target of around 50%. In particular, although the Resona Group announced its intention to allocate an additional JPY15.0 billion to share buybacks, could you provide your rationale for setting this additional budget?

A10. When this fresh budget is combined with our existing budget of JPY10.0 billion announced in May 2023, total funds to be allocated to share buybacks amount to JPY25.0 billion. As stated in page 26 of the IR presentation material, our MMP policy is to aim for a total shareholder return ratio of around 50% even as we continue to deliver a stable dividend stream. Under the previous MMP, we had aimed to achieve this target level over the medium term. However, in line with the current MMP, we aim to accomplish our total shareholder return ratio target of around 50% in the very first year of the plan. Therefore, the setting of the budget for share buybacks is based on our determination to achieve this target.

Q11. Looking at the proportional composition of Group employees vis-à-vis the size of operations run by each Group entity, the number of KMFG employees seems to be disproportionally larger than that of RB and SR. What is your future outlook on employee headcounts?

A11. Indeed, the number of KMFG employees is larger than it should be. We believe that KMFG can achieve further cost reductions in this area.

Under the MMP, we aim to execute the exhaustive overhauling of business processes. Although our business processes are currently supported by a massive workforce of more than 10,000 employees, we will strive to improve this situation, with the aim of shifting management resources to fields of our focus while pursuing cost reductions.

We are facing shortages of human resources in business fields involving sophisticated customer consulting as well as in IT, digital and other fields requiring sophisticated specialist expertise. With this in mind, we will push ahead with business process reforms, which will, in turn, enable us to optimally shift our management resources, while downsizing the overall size of our workforce. This is the general direction of our initiatives.

Q12. Based on the DuPont Analysis, HD's return on risk-weighted assets (RORA) seems to be relatively high in the both aspects of net interest income (NII) and fee income.

If the Resona Group were to aim for further improvement in RORA, although the Group could possibly achieve improvement in NII on the back of interest rate hikes, it also needs to pursue higher profitability through fee income growth. Please name specific business fields in which you aim to pursue expansion in fee income.

Also, do you consider increasing leverage to be a viable option to improve ROE?

A12. Relevant topics are described on pages 9 and 66 of the IR presentation material with the heading of "Financial and Non-Financial Approaches to Improve Corporate Value."

With regard to the pursuit of profit growth, we have set a target of earning additional core income of JPY17.0 billion in the final year of the MMP. In this regard, we have seen many upsides in fields in which we aim for inorganic growth. At the same time, although we have also recognized that some upsides will be available when interest rates rise in fields where we pursue organic growth, these positive factors are mostly excluded from assumptions for the current MMP. On the other hand, whether interest rates rise or not is beyond our control. Accordingly, we will focus on securing greater profit by expanding fee income from such undertakings as consulting while promoting further cost reductions. We are confident of our potential to achieve profit growth in these areas.

As for leverage, our direction is to increase it from the previous level in the course of promoting the effective utilization of capital.

Q13. Please elaborate on topics presented in page 17 of the IR presentation material regarding progress in initiatives related to the financial digital platform (DPF). Did you see any changes in the status of function providers or corporate users?

A13. Given that across-the-board digital transformation (DX) is expected to progress going forward, we consider our financial DPF to have a profound possibility.

As presented in the right middle of page 17 of the IR presentation material, the number of banking app downloads has already exceeded 1 million thanks to the inclusion of customers of Mebuki FG, Hyakujushi Bank and other partners. The balance of fund wrap has been similarly robust, with fund wrap sales recorded by partner banks accounting for approximately 10% of the overall balance that exceeds JPY700.0 billion. Regional financial institutions are facing a diverse range of customer needs. Employing the open API, our financial DPF scheme is capable of accommodating individual needs while offering a highly convenient cafeteria system equipped with flexible options.

From the standpoint of a function provider, we believe that, first and foremost, we need to enhance our platform by creating cases of success within the Resona Group. This is essential to establishing win-win relationships among participants. For example, although we have already released a corporate version of the Group App and received a number of inquiries about it from some regional financial institutions, we aim to first focus on achieving success stories within the Resona Group. In addition, we think that we will be able to considerably develop our mode of providing functions afforded by participants from different sectors, including those related to facial recognition-based individual authorization.

As for the status of user corporations, needs among regional financial institutions differ largely by company. We have engaged in very promising negotiations with some institutions. Moreover, municipal offices could be included in the scope of DPF users going forward as they promote DX. We believe that the Group can take on challenges in these and other new fields.

Q14. Please describe your concepts on the “multi-regional strategy,” a component of the Group’s “one-platform, multi-regional strategy.” Although the Resona Group seems to have positioned the Tokyo metropolitan area and the Kinki area as two key market regions in which it develops its network, does the Group intend to expand its reach outside these regions?

With regard to M&A, banks could be viable candidates for Resona’s counterparts from the perspective of enhancing its customer base and management resources. Please share your thoughts on how your multi-regional strategy should be implemented over the long term.

A14. The Group’s current network consists of the four banks operating on the single platform. In this sense, we can say that our network is already multi-regional.

If the Group were to acquire regional financial institutions via the use of capital, our existing network will work as an overarching frame. Upon acquisition, we will integrate their back-office and other indirect departments to achieve cost reductions while enabling them to take a face-to-face sales approach aligned with characteristics of their respective regional markets. Once successful, M&A of this kind could serve as a model for bank reorganization.

Simultaneously, we will steadfastly serve as a function provider by, for example, making our financial DPF available, in areas that involve no capital utilization.

As discussed above, our initiatives are twofold. In any case, we will first strive to establish our capabilities to provide the "one-platform" irrespective of whether we conduct M&A. We will then go on to develop our multi-regional structure.

Q15. Please elaborate on the sensitivity of the Group's deposit interest rates to hikes in interest rates. When policy rates were upwardly revised the last time in 2006, three domestic megabanks exercised leadership in the banking sector's response. Currently, however, it is unclear how internet-based banks and other financial institutions would react. In addition, while the depositors' previous reaction seemed to have been profoundly affected by the presence of physical branches and ATMs, the retention of their deposits could possibly have become weaker than it used to be due to the widespread use of banking apps. Taking these factors into account, please share your thoughts on the sensitivity of the Group's deposit interest rates.

A15. As exemplified by the collapse of Silicon Valley Bank, depositors are now able to instantly transfer their deposits. This situation is entirely different from that of 20-30 years ago. Moreover, we need to recognize that the popularization of social networking services (SNSs) resulted in the ever-faster proliferation of information.

However, our balance sheet indicates that the average funding cost remains extremely low at 0.004%. This balance sheet is underpinned by our solid deposit base centered on retail customers. In addition, the number of Group App downloads has been steadily amassed to date, reaching 8.5 million. While this app serves as our key non-face-to-face channel, the achievement of 10 million downloads is now in sight. Accordingly, we don't think that our base of individual customer deposits with strong retention could suffer a major collapse. That being said, we need to pay close attention to customer behavior if other banks raise their deposit interest rates considerably. At the same time, we need to deliver new products capable of accommodating diverse customer needs, including those related to user interface (UI) and user experience (UX), in settlement-related fields. We believe that pursuing these and other retail business endeavors aimed at supporting corporate transactions and taking deep root in household finance is another matter of great importance.

Q16. Please elaborate on the status of unrealized losses on yen bonds. While yields on yen bonds are not very likely to turn to negative, holdings of these bonds have no impact on the capital adequacy ratio excluding net unrealized gains on available-for-sale securities, which is one of the Group's target indicators. Although we therefore assume that the impact of these unrealized losses will be negligible, what are your opinions? Could the Group face any negative factors when unrealized gains on these bonds increase?

A16. As you have just pointed out, yen bonds are, unlike foreign bonds, hardly likely to turn into negative yielding bonds at this point of time. Also, we have implemented hedging measures for our holdings of 20-year bonds and other similar instruments. In these and other ways, we have developed foundations for supporting fresh risk-taking endeavors to be launched going forward.

However, we are always aware of the need to take a risk control approach that takes overall status into account. We are entrusted with deposits, which are essential assets of our customers. Accordingly, we need to exercise some degree of overall risk management as we serve as a financial institution supporting the bedrock of indirect financing.

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